DEPARTMENT OF DEFENSE

FISCAL YEAR (FY) 2003 BUDGET ESTIMATES

DEFENSE-WIDE WORKING CAPITAL FUND

DEPARTMENT OF DEFENSE

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OPERATING BUDGET (Cont'd)

DEPARTMENT OF DEFENSE

FISCAL YEAR (FY) 2002 BUDGET ESTIMATES

DEFENSE-WIDE WORKING CAPITAL FUND

DEFENSE-WIDE WORKING CAPITAL FUND
FY 2003 BUDGET ESTIMATES

DEFENSE-WIDE SUMMARY

Defense Agencies will operate nine activity groups within the Defense-Wide Working Capital Fund during FY 2002. The Defense Logistics Agency (DLA) will operate four activity groups; the Defense Finance and Accounting Service (DFAS) and the Defense Information Systems Agency (DISA) will each operate two; and the Defense Security Service (DSS) will operate one.

DFAS was formed in January 1991 from the Military Services finance and accounting functions to improve financial accounting support to DoD-wide activities and to reduce costs by adapting standard policies, procedures, forms, data, and systems; streamlining and consolidating operations; and eliminating redundancies.

DISA was reorganized in 1991 from the former Defense Communications Agency. Its responsibilities include obtaining common telecommunication and information services for command and control and providing assistance in other communication support to meet customer needs.

DLA, formed in the early 1960s, operates the Distribution Depot, Reutilization and Marketing, Supply Management, and Document Automation and Production Service activity groups. Distribution Depots receive, store, and ship inventory. Reutilization and Marketing functions include the reutilization of excess and surplus property and the donation, sale, or disposal of surplus DoD personal property. Supply Management conducts the procurement, inventory management, and technical operations functions for consumable defense inventory. The Document Automation and Production Service provides printing services to customers.

DSS, formerly known as the Defense Investigative Service, was formed in 1972. The mission of DSS is to administer the Personnel Security Investigations (PSI) program and the National Industrial Security Program (NISP) for the Department. The mission of the PSI program is to conduct background investigations on individuals assigned to or affiliated with the Defense Department. The purpose of the NISP program is to ensure that private industry, while performing government contracts, properly safeguards classified information in its possession.

Appropriation Request:

Budgeting and Managing for Results: Full Funding of Retiree Costs: To improve the accounting for and make the cost of government programs more visible to the American people, the Administration is proposing to align the full annual budgetary costs of resources used by programs with the budget accounts that fund the programs. To that end, the budget includes a request for a direct appropriation of $206.9 million for the Working Capital Fund to fund the full accruing cost of the Civil Service Retirement System and retiree health benefits for civilian employees in the Federal Employee Health Benefit Program. Beginning with the FY 2004

Budget, these costs will be build-into the rates charged to Working Capital Fund customers. This proposal does not increase the total costs to the Federal government, since these costs were previously funded from OPM accounts.

By activity group, the requested funding is as follows in millions of dollars:

DLA Supply Management	62.970
DLA Distribution Depots	36.870
Defense Reutilization & Marketing Service	7.640
Document Automation and Production Service	6.105
Defense Finance and Accounting Service	62.699
Defense Information Service Agency	16.189
Defense Security Service	14.406
Total	206.879

ACTIVITY GROUP ANALYSIS
DEFENSE-WIDE WORKING CAPITAL FUND - TOTAL
SOURCE OF NEW ORDERS AND REVENUE
FY 2003 BUDGET ESTIMATES
(Dollars in Millions)

	FY 2001	FY 2002	FY 2003
1. New Orders:			
a. Orders from DoD Components			
Army	4,284.2	4,411.6	4,344.8
Navy	5,260.7	5,405.2	5,199.6
Air Force	6,172.2	6,523.8	6,100.5
Marine Corps	563.1	604.1	613.7
Other	1,967.0	1,549.9	1,705.6
b. Orders from Other Fund Activity Groups	2,443.1	2,663.4	2,825.5
c. Total DoD	20,690.3	21,158.0	20,789.7
d. Other Orders:			
Other Federal Agencies	618.5	699.8	699.5
Trust Fund	0.0	0.0	0.0
Exchange Activities	0.0	0.0	0.0
Non Federal Agencies	312.7	265.9	288.8
Foreign Military Sales	815.0	826.2	862.9
2. Carry-In Orders	1,592.9	1,631.7	1,608.1
3. Total Gross Orders	24,029.4	24,581.6	24,249.0
4. Funded Carry Over	1,643.2	1,582.3	1,555.5
5. DRMS Sales Proceeds	53.9	53.1	47.8
6. Total Gross Sales	22,440.1	23,052.4	22,741.3

DEFENSE-WIDE WORKING CAPITAL FUND
SUMMARY
FY 2003 BUDGET ESTIMATES
REVENUE AND EXPENSES
(Dollars in Millions)

	FY 2001	FY 2002	FY 2003
Revenue:			
Gross Sales	17,515.0	18,152.5	18,588.8
Operations	17,170.2	17,854.0	18,042.1
Capital Surcharge	48.1	0.0	255.9
Depreciation excluding Major Construction	296.7	298.5	290.8
Major Construction Depreciation	0.0	0.0	0.0
ADPE & Telecommunications Equipment	0.0	0.0	0.0
Other Income	410.8	448.8	471.7
Refunds/Discounts (-)	(200.4)	(202.0)	(205.2)
Total Income	**17,725.4**	**18,399.3**	**18,855.3**
Expenses:			
Cost of Materiel Sold from Inventory	8,609.4	9,124.7	9,318.5
Materiel-Related	0.0	0.0	0.0
Salaries and Wages:			
Military Personnel Compensation & Benefits	83.9	82.5	80.2
Civilian Personnel Compensation & Benefits	2,460.7	2,716.1	2,903.4
Travel & Transportation of Personnel	67.4	79.5	78.1
Materials & Supplies (For Internal Oper)	247.0	291.4	302.7
Equipment	31.4	36.5	33.4
Other Purchases from Revolving Funds	1,288.1	1,193.8	1,226.0
Transportation of Things	622.2	616.5	614.5
Major Maintenance & Repair	0.0	0.0	0.0
Depreciation - Capital	290.9	312.4	305.6
Printing & Reproduction	196.9	214.9	218.2
Advisory and Assistance Services	103.9	103.7	129.4
Rent, Communication, Utilities, & Misc.	1,498.8	1,298.6	1,365.1
Other Purchased Services	1,987.5	2,340.4	2,262.7
Total Expenses	**17,488.1**	**18,411.0**	**18,837.8**
Operating Result	**237.3**	**(11.7)**	**17.5**
Less Capital Surcharge Reservation	(48.0)	0.0	(255.9)
Plus Passthroughs or Other Approp Affecting NOR	0.0	0.0	0.0
Other Adjustments Affecting NOR	4.2	(7.6)	78.6
Net Operating Result (NOR)	**193.5**	**(19.3)**	**(159.8)**
Prior Year Adjustments	7.3	0.0	0.0
Other Changes Affecting AOR	165.5	0.5	(70.7)
Prior Year AOR	(98.9)	267.6	248.8
Accumulated Operating Result (AOR)	**267.4**	**248.8**	**18.3**
Non-Recoverable Adjustments Impacting AOR	0.0	0.0	0.0
Accumulated Operating Results for Budget Purposes	**267.4**	**248.8**	**18.3**

DEFENSE-WIDE WORKING CAPITAL FUND
FY 2003 BUDGET SUBMISSION
OVERVIEW

DEFENSE LOGISTICS AGENCY

The Defense Logistics Agency (DLA) is a Combat Support Agency responsible for providing the Military Services with a broad range of logistics support. Responsibilities include the acquisition, storage, and distribution of most of the Department of Defense's (DoD) spare parts and other consumable items, reutilization and marketing of excess military property, document automation services, and operation of the Defense National Stockpile. DLA directly contributes to the warfighting readiness and sustainability of U.S. forces, literally "around the clock - around the world".

Most of these responsibilities are carried out by activity groups operating within the Defense-Wide Working Capital Fund. The DLA portion of the Fund consists of the following four activity groups:

- Supply Management
- Distribution Depots
- Reutilization and Marketing
- Document Automation and Production Service

This submission reflects DLA's continued commitment to execute our DLA 21 goals and implementation of the DLA Strategic Plan through aggressive use of business process reengineering, competitive and strategic sourcing, acquisition reform, and use of emerging technology to reduce infrastructure costs while sustaining readiness support to the warfighter. Specifically, this submission includes:

- ♦ DLA Performance Contract goals and metrics for all major DLA Activity Groups

- ♦ Supply Customer Price Change (CPC) of 3.5 percent in FY 2003

- ♦ Implementation of Net Landed Cost pricing structure for processing workload in the Distribution Depots Activity Group

- ♦ A new pricing structure, Transaction Activity Billings (TAB)for the Defense Reutilization and Marketing Service is used for Service Level Billing (SLB).

- $176.1 million in our capital budget to fund the FY 2003 milestones of the Business Systems Modernization (BSM) initiative

- Full-time equivalent reductions of 9 percent since the beginning of FY 2000 through FY 2003

Detailed highlights by activity group follow:

Supply Management Activity Group

The DLA Supply Management Activity Group incorporates those activities, programs and costs related to material management. Costs include operations (salaries and expenses), material (items sold to the military services) and capital investments (purchase of equipment, software development and minor construction). Approximately twenty million requisitions are received annually from the military services and other federal agencies for the four million consumable items managed by DLA.

The DLA Supply Management Activity Group is broken into wholesale and retail level inventories. Wholesale inventories are inventories the manager has asset knowledge and control over, regardless of funding sources. Retail inventory (or base supply) provides equipment, materials, supplies and services to local DLA activities and authorized tenants. Four Inventory Control Points (ICPs) manage DLA’s wholesale inventories. These ICPs provide the warfighter with Fuel, Troop Support (uniforms, food and medical), General Support (hardware type items), and Weapons Systems Support. DLA’s retail management consists of Base Operating Support (BOS) and the National Security Agency (NSA). In addition, DLA’s Supply management includes a small number of supporting activities, such as the Defense Logistics Information Service (DLIS) and the Defense Automated Addressing Systems Center (DAASC).

In FY 2002, the Defense Energy Support Center will capitalize Aerospace Missile Fuels from the Air Force valued at $131.6 million. DLA is reflecting capitalization of this inventory on inventory exhibits separately from petroleum.

To improve the accounting for and make the cost of government programs more visible to the American people, the Administration is proposing to align the full annual budgetary costs of resources used by programs with the budget accounts that fund the programs. To that end, the budget includes a request for a direct appropriation of $63.0 million for the Working Capital Fund Supply Management Activity Group to fund the full accruing cost of the Civil Service Retirement System and retiree health benefits for civilian employees in the Federal Employee Health Benefit Program.

Beginning with the FY 2004 budget, these costs will be built into the rates charged to Working Capital Fund customers. This proposal does not increase the total costs to the Federal government, since these costs were previously funded from a central account.

Based upon the DLA's FY 2000 Performance Contract commitments, DLA was tasked to determine how to achieve a weapon system supply availability goal of 85 percent for each of the Military Services. Although DLA is already achieving an aggregate weapon system supply availability of 85 percent, Air Force and Navy support is below that level. Analysis has indicated that overall supply availability is being negatively impacted by items related to aviation support. To improve the availability of aviation spare parts, $500 million in appropriated funding is included in the Air Force and Navy Operations and Maintenance accounts for additional support beginning in FY 2001 through FY 2004. The *appropriated* amounts included are $100 million, $147.9 million, $133.1 million and $119 million, respectively, per fiscal year. DLA will procure $334 million in aviation spare parts, $120 million in aviation engine spares and $46 million to support aviation non-demand items. Procurement actions began in FY 2000.

Defense Logistics Information Service is resourced through a Service Level Billing (SLB) to each DoD Supply Management Activity Group (Army, Navy, Air Force and DLA). The services provided by DLIS are Information Management (IM), Information Dissemination (ID) and Cataloging. In FY 2003 the method for allocating the SLB is an equal allocation for IM; customer usage for ID; and the number of national stock numbers managed for Cataloging. This method is commonly referred to as the Primary Inventory Control Activity (PICA). Costs are increased across budget years to reflect increased Defense Information Systems Agency costs and a conversion effort for Catalog Reengineering and Customer Relations Management.

The Defense Automated Addressing Systems Center is also financed via a service level billing, with each Supply Management Activity financing an equal portion of DAASC's costs. DAASC cost increases are attributable to software maintenance increases, Information Assurance, Core Mapping Sustainment, and Logistics Data Gateway.

Commitment Authority is the administrative reservation of funds for future obligations. It allows additional obligations on a dollar-for-dollar basis when customer orders (demands) increase, or when prices, such as fuel prices, rise during the fiscal year. The FY 2002 amount is based on FY 2001 execution plus an additional $2.1 billion in anticipation of support for world events since September 11, 2001. FY 2003 is based on FY 2001 execution.

On May 10, 2000, the Court of Federal claims awarded Pride

Companies, L.P. $45.7 million because of an unauthorized price adjustment clause in Pride's contracts providing refined fuel products from 1987 – 1992. With interest, the total payment was $61.5 million. Pride was paid in FY 2000. Claims arising from the Pride Companies decision have been filed; however, none are at the point to include in this budget estimates submission. The Pride case is not expected to be a precedent for future cases.

The Customer Price Change (CPC) is the average change in price from one year to the next that the customer will encounter for the average non-energy item. DLA's goal is to have a CPC of no greater than the DoD composite inflation factor. Changes in customer price are driven by factors such as: inflation, basic costs incurred to procure, store, and ship to the customer; and possibly other DoD decisions. The FY 2001 increase was primarily due to the DoD decision to fully finance the Defense Reutilization and Marketing Service (DRMS) ($252.7 million) solely in the DLA Supply Non-Energy prices rather than sharing this cost with the Army, Navy, and Air Force. That decision was revisited and DRMS costs are financed on a shared cost basis in FY 2002 and FY 2003. The FY 2003 increase is attributed to a capital surcharge to finance the costs of Business Systems Modernization.
The Cost Recovery Rate (CRR) or surcharge is the additive amount to the price of an item for purchasing and selling supplies to the customer. These costs include operating costs such as compensation, benefits, travel, training, depreciation, facilities maintenance, and service charges for shipping and storage, accounting, cataloging, and disposal. The CRR for FY 2003 is 20.7%. For this submission, several changes have been made to the CRR and are explained in detail in the Supply Activity Group narrative.

The Office of Management and Budget establishes fuel rates with input from the Departments of Defense, Energy, Treasury, and Commerce. The single most important cost factor is the world petroleum market price/product cost. While this product cost is outside DLA's direct control, several acquisition and materiel management techniques are used to mitigate rising costs. Acquisition techniques include flexible (seasonal or spot) buying, dollar cost averaging, market sensitive ordering, commercial buying of bunker fuels, minimal small and disadvantaged business premium payments, and the increased use of commercial specifications. Materiel management techniques include improved requirements forecasting and using refinery production capacity in place of product to support the Military Services War Reserve requirement. Additionally, DLA is continually changing its storage and transportation methods in search of efficiencies without impeding petroleum support effectiveness. The FY 2000 Emergency Supplemental provided $1,556.2 million to cover the cost of inflation for bulk petroleum purchased by DoD, of which $800 million was returned to the Military Services in FY 2001, as specified by Congress. The FY 2003 fuel standard unit price is net of $100 million provided through direct appropriation in the Defense Emergency Response Fund.

Activity Group Profile

	($ in Millions)		
	FY 2001	FY 2002	FY 2003
Cost of Goods Sold	$13,179.6	$12,301.2	$12,554.0
Net Operating Results	$-963.1	$863.9	$-37.6
Accumulated Operating Results	$-978.2	$-114.3	$-151.9
Civilian End Strength	11,091	11,561	11,629
Military End Strength	370	371	371
Civilian Full-Time Equivalents	10,746	11,376	11,492
Military Workyears	370	371	371
Capital Budget Program Authority	$176.8	$165.0	$268.8

Distribution Depots Activity Group

The Defense Logistics Agency (DLA) Distribution Depot Activity Group is responsible for the global distribution and warehousing of Military Service and DLA line items. These items consist of wholesale DoD weapon systems parts and other defense related consumable items to include medical, clothing, subsistence, electrical, industrial and general supplies. In FY 2001, the distribution depots, by location and component are:

DLA
Columbus, OH
San Joaquin, CA
Richmond, VA
Susquehanna, PA
Germersheim, Germany
Map Support, Richmond, VA

Navy
Cherry Point, NC
San Diego, CA
Jacksonville, FL
Norfolk, VA
Puget Sound, WA
Pearl Harbor, HI
Yokosuka, Japan

Marines
Albany, GA
Barstow, CA

Army
Anniston, AL
Corpus Christi, TX
Red River, TX
Tobyhanna, PA

Air Force
Hill, UT
McClellan, CA
Oklahoma City, OK
Warner Robins, GA
San Antonio, TX

These depots strategically located throughout the world, received and issued almost 23 million secondary lines and warehoused and maintained over 225 million cubic feet of material. The Defense Distribution Depot network insures that America’s war fighters receive the best value in distribution services by providing “around the clock - around the world” world-class service for the least cost to the taxpayers. All items are typically prepared and shipped within one day of receiving the shipping order.

Since FY 1998, the Distribution Depot Activity Group has made great strides in reducing infrastructure, eliminating duplicate functions, and streamlining the way we do business. Examples of these efforts include:

- Reengineering DLA's Strategic Distribution Platforms (SDPs) located at the Defense Distribution Depot San Joaquin California, and at the Defense Distribution Depot Susquehanna Pennsylvania. At both SDPs, the reengineering efforts involved rewarehousing material from nearby facilities and eliminating duplicate functions. These actions resulted in the reduction of more than 700 employees and a substantial increase in productivity at the two sites.

- Closing the two remaining Base Realignment and Closure (BRAC) depots, Distribution Depot San Antonio, TX, and Distribution Depot McClellan, CA in July 2001. The closure of these last two facilities completed facility reductions to the Distribution Activity Group under existing BRAC legislation.

- Completing the A-76 competition of the first five of sixteen depots with private industry.

    - The first competition award announced in November 1999, resulted in the Defense Distribution Depot Columbus, OH retaining depot operations and management in house.
    - The next two competition awards announced January 2000 for the Defense Distribution Depot Barstow, CA (DDBC) and February 2000 for the Defense Distribution Depot Warner Robins GA, resulted in contracting out the operations and management functions for both depots to EG&G Logistics, Inc.
    - The last two competition awards announced to date were for the Defense Distribution Depot Jacksonville, FL during March 2001, and the Defense Distribution Depot Cherry Point, NC during May 2001. These depots were contracted out to MANCON of Virginia Beach, VA and LABAT-Anderson of McLean, VA, respectively.

    On January 11, 2002 the Defense Distribution Depot Richmond, VA competition resulted in a tentative decision to retain depot operations and management in house.

Three additional competitions are pending tentative decisions in FY 2002: Defense Distribution Depot San Diego, CA; Defense Distribution Depot Hill, UT; and Defense Distribution Depot Albany, GA. The process follows federal policy for deciding whether to retain recurring, commercial-like activities within the government or contract them out to a private sector source. The goal of the program is to reduce costs through the competitive process and through process reengineering. These competitions will provide quality support and significant cost savings to the war fighters in the years to come.

DLA announced competition of the seven remaining Continental United States depots during October 2001. We expect decisions on four of the depots in FY 2003 and decisions on the remaining three depots in FY 2004. We will announce the two final studies of the support functions at the SDPs at the end of FY 2002.

Estimated cost assumptions/savings for the competitions are as follows:

- Study costs estimated at $4,000 per full-time equivalent (FTE);
- Severance costs for personnel reductions and contract conversions for half of the depots being studied estimated at $28,000 per FTE.
- Savings reflect an increase to a net 25%.

FTE and labor savings budgeted include only most efficient organization (MEO) savings. Costs and savings are prorated to the fiscal year in which they are expected to occur. The entire A-76 process should be completed by the end of FY 2005.

The metrics for this activity group are outlined in the Performance Contract. These metrics include: (1) operating results; (2) competitions for depots; (3) unit costs for distribution services, (4) total cost for distribution services; (5) inventory accuracy for products, (6) location accuracy for products; and (7) customer satisfaction index. These metrics establish minimum performance targets for this Activity group in order to achieve or exceed established targets.

Consistent with activity based costing techniques, in FY 2002, DLA implemented the Net Landed Cost pricing mechanism at the Distribution Depots. Net Landed Cost provides our customers with visibility of their distribution costs by commodity, customer, and transactions so that they may make more informed supply decisions as well as develop more accurate surcharges.

The previous pricing methodology did not reflect the varying levels of distribution services rendered. Customers were not aware of the cost implications of specifying either routine; priority; special levels/value of added services; or cost drivers of the varying materiel DLA handles. The use of average line item costs did not reflect the actual level of effort expended with respect to individual items processed. Without this level of detail, precise costs cannot be determined and subsequently used as a mechanism for developing competitive prices.

As the next step in the process of aligning costs more accurately, we have applied our ABC techniques to the cost drivers for the storage mission and have realigned our costs to apply Net Landed Cost to the Storage mission. During FY 2001, we executed an intense program to correct storage data, specifically item weight and cube. This initiative measures the actual size of an item rather than the space it occupies in the depot. In doing so, there have been some shifts in costs between customers. These shifts are a more accurate reflection of the true costs of our business processes by appropriate customer.

To date, overall performance has improved while costs continue to decrease. Continuing process efficiencies, steady drops in mission workload and contracting out depot workload have led to significant reductions to the distribution workforce. Endstrength dropped from 25,372 in FY 1992 to a projected 8,357 in FY 2003, a reduction of 17,015 personnel, or a 67 percent decrease. Reductions to date have been accomplished mainly through the use of Voluntary Separation Incentive Pay (VSIP) and Voluntary Early Retirement Authority (VERA). Various Reductions-in-Force (RIFs) conducted during FY 2001 resulted in 79 separations. To maintain the appropriate balance of workforce to workload, additional RIFs will be conducted, as necessary, during FYs 2002/2003.

To improve the accounting for and make the cost of government programs more visible to the American people, the Administration is proposing to align the full annual budgetary costs of resources used by programs with the budget accounts that fund the programs. To that end, the budget includes a request for a direct appropriation of $36.9 million for Distribution to fund the full accruing cost of the Civil Service Retirement System and retiree health benefits for civilian employees in the Federal Employee Health Benefit Program. Beginning with the FY 2004 Budget, these costs will be built into the rates charged to Working Capital Fund customers. This proposal does not increase the total costs to the Federal government, since these costs were previously funded from a central account.

Since inventory managers began paying for storage in FY 1996, storage volume at the depots has decreased. The FY 2003 estimate reflects Net Landed Cost (NLC) for storage based on item cubic feet. The correction of storage data through a joint Service effort resulted in more accurate item cube data. Using NLC, DLA will bill the customer for material (based upon total item cube) stored in our warehouses. In so doing, we will fully automate a previously manual process and will bring storage billing into real-time billing vice billing based on prior period workload. This visibility allows our customers, to determine the level of inventory they want to maintain in DLA storage. We expect a continued decrease in workload in this business area as a result of continued scrutiny of storage data reports and initiatives to maximize use of commercial vendor stocks.

As stated previously, we have applied our ABC techniques by looking at the cost drivers for storage and have realigned our costs accordingly. Because the workload is decreasing faster than costs, and because storage charges are built on prior-year workload averaging, we have incorporated Net Landed Cost (cost per item cube) in FY 2003. While the FY 2003 storage rate to customers is over two-thirds higher, conversely the workload is almost two-thirds lower. Total costs remain the same. In addition, we have added an additional rate, Specialized Storage, for those items in controlled facilities, such as hazardous, controlled humidity, chill vault, freeze and flammable warehouse facilities.

The last two depots closed under BRAC in FY 2001, left an infrastructure still in excess of distribution depot requirements. To the extent possible, we are continuing to vacate warehouses and return them to hosts/owners. Only through reduced inventory can we reduce our fixed costs – infrastructure – and pass these savings to our customers. With Net Landed Cost for storage, our customers will be provided item cube data at the national stock number level by distribution center, which will help the customer make better sourcing decisions.

Activity Group Profile

	($ in Millions)		
	FY 2001	FY 2002	FY 2003
Cost of Goods Sold	-	-	-
Net Operating Results	$-11.9	$-73.8	$0.5
Accumulated Operating Results	$73.3	$-0.5	$0.0
Civilian End Strength	8,989	8,906	8,357
Military End Strength	177	178	178
Civilian Full-Time Equivalents	9,052	8,929	8,430
Military Workyears	177	178	178
Capital Budget			

Program Authority	$40.7	$32.1	$51.3

Reutilization and Marketing Activity Group

The Defense Logistics Agency (DLA) Defense Reutilization and Marketing Service (DRMS) Activity Group is responsible for the reuse, or reutilization, of excess and surplus personal property within the Department of Defense (DoD). Items received by the DLA Defense Reutilization and Marketing Offices (DRMOs) meeting Military Services item manager criteria are automatically referred through front-end screening notices. The Military Services reutilized approximately $1.4 billion worth of personal property in FY 2001, resulting in savings to the DoD and the Government. If property is not reutilized, it can be transferred to other Federal agencies. Remaining property becomes surplus and is made available for donation to authorized state agencies and charitable organizations. The balance of property is offered for competitive sale to the public.

The DLA disposal mission includes hazardous property disposition. In this capacity, DLA handles the vast majority of DoD property governed by the Resource Conservation Recovery Act (RCRA) of 1976, as amended. Some hazardous material has reutilization and/or sales value and goes through the same process as all other DoD property. However, once it has been screened for potential reutilization or sales value, all hazardous waste is directly disposed of through contracts managed by DLA and funded by the Military Services.

DRMS headquarters, responsible for operational control, is located in Battle Creek, Michigan. The operational core of this organization lies with individual DRMOs located on military installations throughout the world. DRMOs receive, classify, segregate, demilitarize, account for and report excess material for screening, lotting, merchandising, and sales.

The organization is at the halfway point in a transformation that by 2005 will result in an entity little more than one-third of its 1996 size. Throughout this transformation, DRMS is maintaining quality service to its customers, but delivering these services through innovative contracts and more effective use of information technology.

DRMS recognizes that disposal workload has and probably will continue to decline. In response to this workload decline, DRMS eliminated over 1,500 FTEs between FY 1997 and FY 2001 and projects continued reductions of 384 FTEs over the budget period. The projected FTE reduction outpaces the decline in workload due to initiatives that have resulted in more streamlined work processes and the movement of commercial type processes to the private sector. The number of line items received from FY 1997 through FY

2005 is projected to decrease at an average annual rate of five percent per year while FTEs are programmed to decrease at an average annual rate of eight percent per year. This results in an average annual increase in productivity of seven percent per year. DRMS also does not plan to retain the current DRMO infrastructure. DRMS reduced the number of DRMOs in the continental United States (CONUS) by approximately one-half in an Infrastructure Reduction initiative begun in late FY 1997. This was a major task, which took two years to complete.

DRMS also conducted an A-76 public/private competition on the logistics stock, store and issue functions at 10 DRMOs. The first DRMS A-76 competition was completed in FY 2000 and resulted in the conversion to contract of the affected functions. DRMS is proceeding with a second A-76 competition of the warehouse logistics functions at the 61 CONUS DRMOs not yet studied. DLA issued the public announcement of the A-76 competition on October 9, 2001. It will impact approximately 400 FTEs.

DRMS has a long-range goal of becoming a broker of information, which will result in the more efficient management of property. Initiatives have been focused on enacting process improvements that will allow DRMS to better achieve this goal. As DRMS transitions to an organization that is more adept at “moving information and not property”, DRMS will be able to centralize its organizational presence at fewer strategic locations. This will allow DRMS to perform its mission with substantially reduced infrastructure, labor and cost.

Historically, DRMS has recovered operating costs with a combination of proceeds from the sale of surplus personal property to the public, reimbursements from specific customers for work performed and a Service Level Billing (SLB) paid by the Military Services and DLA Supply Management Activity Groups. DLA developed Transaction Activity Billing (TAB) to recover mission costs through a process that provides customers (Military Services and DLA) bills based on actual services and workload for property disposition. Estimated workload and cost data are processed through the TAB model. Through this process, DRMS can identify the end user and the working capital fund customer separately, providing visibility of the disposal cost in the life cycle of the item.

By having visibility of the cost for various services that DRMS provides, customers can influence their costs. TAB is a practical application of Activity Based Costing (ABC) principles to assess costs and set rates in accordance with the level of effort required to perform the service. DRMS implemented the system and began testing in FY 2001, and we will use FY 2002 data to validate the application of the TAB rates and workload estimates. In FY 2003 the SLB is based on TAB rates and workload estimates.

DRMS is changing processes and investing in technology to enable decreased reliance on physical infrastructure. As DRMS makes the transition from performing disposal with a network of warehouses and scrapyards to managing information with no movement of the property until the final disposition is determined, the cost to physically turn property in to a DRMO will increase. The additional cost of physical turn in versus electronic turn in (Received in Place) should give DRMS' customers a financial incentive to decrease their reliance on the DRMS' physical infrastructure.

In FY 2001, DRMS experienced an NOR gain of $57.1 million. This gain partially offsets the AOR loss brought forward from the FY 2000 revenue loss incurred. This loss was the result of an unsuccessful legislative proposal to allow the transfer of revenue from the Defense National Stockpile Center to DRMS, in lieu of a Military Service/DLA-financed Service Level Billing to finance DRMS operating costs. During FY 2002, DRMS will bill its customers at the SLB amount set in the last budget cycle. These SLB amounts were based on TAB workload estimates and recoverable costs. For FY 2003, DRMS costs not covered by other revenue (sales, reimbursable projects) will be recovered again based on the SLB as determined by TAB costs and workload estimates.

Activity Group Profile

	($ in Millions)		
	FY 2001	FY 2002	FY 2003
Cost of Goods Sold	$338.1	$332.6	$314.4
Net Operating Results	$57.1	$58.2	$51.5
Accumulated Operating Results	$-109.7	$-51.5	$0.0
Civilian End Strength	1,932	1,776	1,630
Military End Strength	9	9	9
Civilian Full-Time Equivalents	2,088	1,855	1,704
Military Workyears	9	9	9
Capital Budget Program Authority	$6.3	$12.8	$8.1

Document Automation and Production Service Activity Group

The Document Automation and Production Service (DAPS) is responsible for the DoD printing, duplicating, and document automation programs. This responsibility encompasses the full range of automated printing services to include: conversion, electronic storage and output, and the distribution of hard copy and digital information. DAPS provides time sensitive, competitively priced, high quality products and services that are produced either in-house or procured through the Government Printing Office (GPO).

DAPS manages this worldwide mission through a customer service network comprised of a Headquarters located at Mechanicsburg, Pennsylvania, 80 major field locations and 185 smaller document automation facilities.
DAPS continues to make every effort to streamline its operations and make process improvements to reduce costs. Since becoming the Department's manager for printing and duplication in 1992, DAPS closed or consolidated approximately 200 printing facilities

A recent process improvement, involves the use of the DAPS "merchant status". This allows DAPS to accept International Merchant Purchase Authorization Cards (IMPAC) from all customers. Use of the IMPAC card reduces a customer's administrative and DFAS costs. During FY 2001, over $129 million in products and services were purchased using IMPAC cards.

In addition to streamlining operations, DAPS has increased its customer base. In March 2001, U.S. Army Printing Facilities in the Republic of Korea transferred to DAPS. DAPS provides its traditional services as well as mobilization support for the Army. The Army was projected to have annual operating savings in FY 2001 of $70 thousand and $120 thousand in both FY 2002 and FY 2003.

In FY 2001 DAPS established a memorandum of agreement (MOA) with the department of the Navy, to act as the issuing agent for the Smart /Common Access Card Program. DAPS will provide this service for afloat and ashore units to include Active Duty, Selected Service Reservists, and Civilians. DAPS received initial funding of $0.6 million from the Department of the Navy.

DAPS signed an MOA with the National Institute of Health (NIH) to provide digital print document conversion services for NIH grant applications. Implementation is in two phases, phase 1 began in March 2001, and the second phase will begin in March of 2002. When fully implemented, DAPS will receive additional annual revenue in excess of $2.5 million. DAPS received revenue of $0.6 million in FY 2001. DAPS anticipates receiving $1.9 million in FY 2002 and after full implementation, $2.5 million in FY 2003.

DAPS will provide an Enterprise Document Management System to the Defense Distribution Center (DDC). The project will support 21 DDC centers. The system assists customers in records requirements, including conversion to digital format, data storage, and data access. The system will improve document retrieval, automate indexing for shipping and receiving and provides a single digital format, and central database. Implementation will begin in FY 2002.

DAPS did not achieve its unit cost goal due to the reduction in workload. “Hard copy” pages fell 13 percent from FY 2000 through FY 2001. The hard copy pages are one of the largest unit cost drivers for DAPS. There was an increase in document electronic conversion however this type of workload is more costly than hard copy. While electronic conversion may be more costly for DAPS in the short term, there will be long term cost savings for DoD. DAPS workload reflects the transition of the Department from “hard copy” to digital documents. The number of pages converted to digital by DAPS in FY 2001 increased by 32.7 percent or 20 million pages from FY 2000 to a total of 61.3 million. This trend is expected to continue through the budget year resulting in a decrease in total units and increase in unit cost.

DAPS finished FY 2001 with a positive NOR of $0.3 million against a goal of $23.1 million. This shortfall is due to lower than planned workload and ultimately lower revenue. Other appropriations affecting NOR, $0.2 million, was due to the Department receiving congressional funding for increased utility costs. A series of accounting adjustments to reverse outstanding and invalid accounts payable resulted in a prior year AOR adjustment of $7.3 million. The NOR for FY 2002 is $5.6 million and for FY 2003, it is $10.1 million. Other Appropriations affecting NOR, $6.1 million, is the result of full funding of retiree costs.

To improve the accounting for and make the cost of government programs more visible to the American people, the Administration is proposing to align the full annual budgetary costs of resources used by programs with the budget accounts that fund the programs. To that end, the budget includes a request for a direct appropriation of $6.1 million for DAPS to fund the full accruing cost of the Civil Service Retirement System and retiree health benefits for civilian employees in the Federal Employee Health Benefit Program. Beginning with the FY 2004 budget, these costs will be built into the rates charged to Working Capital Fund customers. This proposal does not increase the total costs to the Federal government, since these costs were previously funded from a central account.

DAPS continues to right size its workforce to reflect changes in workload and facility consolidations. This submission reflects full-time equivalent reductions of 9 percent in FY 2001, 6 percent in FY 2002, and 6 percent in FY 2003. These full-time equivalent reductions will continue in an effort to align the workforce with workload.

Activity Group Profile

	($ in Millions)		
	FY 2001	FY 2002	FY 2003
Cost of Goods Sold	$389.9	$394.4	$406.3
Net Operating Results	$0.5	$5.6	$16.2
Accumulated Operating Results	$-21.8	$-16.2	-
Civilian End Strength	1,438	1,300	1,229
Military End Strength	0	0	0
Civilian Full-Time Equivalents	1,469	1,374	1,289
Military Workyears	0	0	0
Capital Budget Program Authority	$4.7	$9.2	$11.3